

**REPORT OF THE AUDITOR-GENERAL TO THE MPUMALANGA LEGISLATURE AND  
THE COUNCIL ON THE FINANCIAL STATEMENTS AND PERFORMANCE  
INFORMATION OF THE NKOMAZI LOCAL MUNICIPALITY FOR THE YEAR ENDED  
30 JUNE 2009**

**REPORT ON THE FINANCIAL STATEMENTS**

1. I have audited the accompanying financial statements of the Nkomazi Local Municipality which comprise the statement of financial position as at 30 June 2009, and the statement of financial performance, the statement of changes in net assets and the cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages [xx] to [xx].

**The accounting officer's responsibility for the financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the Statements of Generally Recognised Accounting Practice (Statements of GRAP) and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

**The Auditor-General's responsibility**

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with the International Standards on Auditing read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
6. Paragraph 11 *et seq.* of the Statement of Generally Recognised Accounting Practice, GRAP 1 *Presentation of Financial Statements* requires that financial reporting by entities shall provide information on whether resources were obtained and used in accordance with the legally adopted budget. As the budget reporting standard is not effective for this financial year, I have determined that my audit of any disclosures made by the Nkomazi Local Municipality in this respect will be limited to reporting on non-compliance with this disclosure requirement.
7. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.



## **Basis for qualified opinion**

### **Biological assets**

8. In terms of paragraph 15 of GRAP 101 *Agriculture*, biological assets must be revalued at every reporting date at their fair value less estimated point of sale. The municipality did not revalue the biological assets of R12 105 777 as disclosed in note 2 to the financial statements as at 30 June 2009. These biological assets as well as the accumulated surplus as disclosed in the statement of changes in net assets were therefore misstated. As the municipality did not perform a physical count of the biological assets at the reporting date, it was impracticable to quantify the effect of this misstatement.

### **Provision for landfill site**

9. In terms of paragraph 25 of GRAP 17 *Property, Plant and Equipment*, the cost of an item of property, plant and equipment includes the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period. A provision for landfill sites was not maintained by the municipality during the year under review as required. It was impracticable to quantify the effect of the misstatement, as no reporting information was available to determine the amount.

### **Property, plant and equipment**

10. Sufficient appropriate audit evidence could not be obtained as to the existence, rights, completeness and valuation of infrastructure assets, as disclosed in note 4 to the financial statements to the carrying value of R518 785 934 for the current financial year, due to the incomplete classification of assets in the fixed asset register. I was unable to perform suitable alternative procedures, due to the poor quality of the fixed asset register, including a lack of descriptions, locations, asset numbers and/or bar codes.
11. Supporting documentation was not submitted for additions to property, plant and equipment to the value of R1 625 712 included in the closing balance of property, plant and equipment, as disclosed in note 4 to the financial statements. Therefore, I was unable to confirm the completeness, valuation and existence of these additions. I was unable to perform alternative procedures, as the municipality's financial system did not provide detailed descriptions of these transactions.

### **Revenue**

12. Distribution losses of electricity for the 2008-09 financial year were not determined. As a result, I could not obtain sufficient appropriate audit evidence as to the completeness and accuracy of the accounting records beyond the actual receipts recorded, and therefore revenue from the sale of electricity to the amount of R24 202 020 as disclosed in note 21 to the financial statements.

### **Fruitless and wasteful expenditure**

13. An overpayment of R3 245 000 was made to a supplier, as the tender amount was exceeded. The municipality did not disclose this fruitless and wasteful expenditure in the financial statements, contrary to the requirements of section 125(2)(d) of the MFMA.

## **Qualified opinion**

14. In my opinion, except for the possible effects of the matters described in the Basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Nkomazi Local Municipality as at 30 June 2009 and its financial performance and its cash flows for the year then ended, in accordance with the Statements of GRAP and in the manner required by the MFMA.

### Emphasis of matter

I draw attention to the following matter on which I do not express a qualified opinion:

#### Restatement of corresponding figures

15. As disclosed in note 30 to the financial statements, the corresponding figures for 30 June 2008 have been restated as a result of an error discovered during the current financial year in the financial statements of the municipality at, and for the year ended, 30 June 2008.

### Other matters

#### Unaudited supplementary schedules

16. The municipality provided supplementary information in the financial statements on whether resources were obtained and used in accordance with the legally adopted budget, in accordance with GRAP 1 *Presentation of Financial Statements*. The supplementary budget information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. Accordingly I do not express an opinion thereon.

### Governance framework

17. The governance principles that impact the auditor's opinion on the financial statements are related to the responsibilities and practices exercised by the accounting officer and executive management and are reflected in the internal control deficiencies and key governance responsibilities addressed below:

#### Internal control deficiencies

18. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes that gave rise to the deficiencies in the system of internal control, which led to the qualified opinion. The root causes are categorised according to the five components of an effective system of internal control. In some instances deficiencies exist in more than one internal control component.

Par. no.	Basis for qualified opinion	CE	RA	CA	IC	M
8	Biological assets	5	2	3	3	1
9	Landfill site provision	5	2	3	3	1
10-11	Property, plant and equipment	5	2	3	3	1
12	Revenue	5	2	3	3	1
13	Fruitless and wasteful expenditure	5	2	3	3	1
14	Irregular expenditure	5	2	3	3	1

19. Oversight was not achieved by the accounting officer through exercising responsibility over financial reporting as well as identifying risks to achieve the financial reporting objectives. Controls had not been designed to ensure that transactions were complete and accurately processed throughout the year. Due to the fact that the deputy CFO was suspended, ongoing monitoring and supervision were not undertaken.

Legend	
CE = Control environment	
The organisational structure does not address areas of responsibility and lines of reporting to support effective control over financial reporting.	1



Management and staff are not assigned appropriate levels of authority and responsibility to facilitate control over financial reporting.	2
Human resource policies do not facilitate effective recruitment and training, disciplining and supervision of personnel.	3
Integrity and ethical values have not been developed and are not understood to set the standard for financial reporting.	4
The accounting officer does not exercise oversight responsibility over financial reporting and internal control.	5
Management's philosophy and operating style do not promote effective control over financial reporting.	6
The entity does not have individuals competent in financial reporting and related matters.	7
<b>RA = Risk assessment</b>	
Management has not specified financial reporting objectives to enable the identification of risks to reliable financial reporting.	1
The entity does not identify risks to the achievement of financial reporting objectives.	2
The entity does not analyse the likelihood and impact of the risks identified.	3
The entity does not determine a risk strategy/action plan to manage identified risks.	4
The potential for material misstatement due to fraud is not considered.	5
<b>CA = Control activities</b>	
There is inadequate segregation of duties to prevent fraudulent data and asset misappropriation.	1
General information technology controls have not been designed to maintain the integrity of the information system and the security of the data.	2
Manual or automated controls are not designed to ensure that the transactions have occurred, are authorised, and are completely and accurately processed.	3
Actions are not taken to address risks to the achievement of financial reporting objectives.	4
Control activities are not selected and developed to mitigate risks over financial reporting.	5
Policies and procedures related to financial reporting are not established and communicated.	6
Realistic targets are not set for financial performance measures, which are in turn not linked to an effective reward system.	7
<b>IC = Information and communication</b>	
Pertinent information is not identified and captured in a form and time frame to support financial reporting.	1
Information required to implement internal control is not available to personnel to enable internal control responsibilities.	2
Communications do not enable and support the understanding and execution of internal control processes and responsibilities by personnel.	3
<b>M = Monitoring</b>	
Ongoing monitoring and supervision are not undertaken to enable an assessment of the effectiveness of internal control over financial reporting.	1
Neither reviews by internal audit or the audit committee nor self-assessments are evident.	2
Internal control deficiencies are not identified and communicated in a timely manner to allow for corrective action to be taken.	3

### Key governance responsibilities

20. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of key governance responsibilities, which I have assessed as follows:

No.	Matter	Y	N
<b>Clear trail of supporting documentation that is easily available and provided in a timely manner</b>			
1.	No significant difficulties were experienced during the audit concerning delays or the availability of requested information.	Y	
<b>Quality of financial statements and related management information</b>			
2.	The financial statements were not subject to any material amendments resulting from the audit.		N
3.	The annual report was submitted for consideration prior to the tabling of the auditor's report.	Y	
<b>Timeliness of financial statements and management information</b>			
4.	The annual financial statements were submitted for auditing as per the legislated deadlines (section 126 of the MFMA).	Y	
<b>Availability of key officials during audit</b>			
5.	Key officials were available throughout the audit process.	Y	



No.	Matter	Y	N
<b>Development of and compliance with risk management, effective internal control and governance practices</b>			
6.	Audit committee		
	<ul style="list-style-type: none"> <li>The municipality had an audit committee in operation throughout the financial year.</li> </ul>		N
	<ul style="list-style-type: none"> <li>The audit committee operates in accordance with approved, written terms of reference.</li> </ul>	Y	
	<ul style="list-style-type: none"> <li>The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA.</li> </ul>		N
7.	Internal audit		
	<ul style="list-style-type: none"> <li>The municipality had an internal audit function in operation throughout the financial year.</li> </ul>	Y	
	<ul style="list-style-type: none"> <li>The internal audit function operates in terms of an approved internal audit plan.</li> </ul>	Y	
	<ul style="list-style-type: none"> <li>The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA.</li> </ul>		N
8.	There are no significant deficiencies in the design and implementation of internal control in respect of financial and risk management.		N
9.	There are no significant deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations.		N
10.	The information systems were appropriate to facilitate the preparation of the financial statements.		N
11.	A risk assessment was conducted on a regular basis and a risk management strategy, which includes a fraud prevention plan, is documented and used as set out in section 62(1)(c)(i) of the MFMA.	Y	
12.	Delegations of responsibility are in place, as set out in section 79 of the MFMA.	Y	
<b>Follow-up of audit findings</b>			
13.	The prior year audit findings have been substantially addressed.	Y	
14.	SCOPA resolutions have been substantially implemented.	Y	
<b>Issues relating to the reporting of performance information</b>			
15.	The information systems were appropriate to facilitate the preparation of a performance report that is accurate and complete.		N
16.	Adequate control processes and procedures are designed and implemented to ensure the accuracy and completeness of reported performance information.		N
17.	A strategic plan was prepared and approved for the financial year under review for purposes of monitoring the performance in relation to the budget and delivery by the municipality against its mandate, predetermined objectives, outputs, indicators and targets in terms of section 68 of the MFMA.	Y	
18.	There is a functioning performance management system and performance bonuses are only paid after proper assessment and approval by those charged with governance.		N

21. Based on the assessment of the governance framework, the audit committee did not meet at least four times during the year and therefore did not perform its functions

throughout the year. Furthermore, the internal audit unit needs more staff to execute its audit plan during the year and report to the audit committee.

### **Investigations**

22. An investigation is being conducted regarding the suspended municipal manager. The investigation had not been concluded at the date of this report.

## **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

### **Report on performance information**

23. I have reviewed the performance information as set out on pages xx to xx.

### **The accounting officer's responsibility for the performance information**

24. In terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality, prepared by the municipality in terms of section 46 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

### **The Auditor-General's responsibility**

25. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008* and section 45 of the MSA.
26. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.
27. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the findings reported below.

### **Findings on performance information**

#### **Non-compliance with regulatory requirements**

##### **Lack of implementation of a performance management system**

28. The municipality did not implement a framework that describes and represents how the municipality's cycle and processes of performance planning, monitoring, measurement, review, reporting and improvement will be conducted, organised and managed, including determining the roles of the different role players, as required in terms of regulations 7 and 8 of the Municipal Planning and Performance Management Regulations, 2001.

##### **No mid-year budget and performance assessments**

29. The accounting officer of the municipality did not by 25 January 2009 assess the performance of the municipality during the first half of the financial year, taking into account the municipality's service delivery performance during the first half of the financial year and the service delivery targets and performance indicators set in the service delivery and budget implementation plan, as required by section 72 of the MFMA.

##### **Existence and functioning of a performance audit committee**

30. The performance audit committee did not:



- meet at least twice during the financial year
- review the quarterly reports of the internal auditors on their audits of the performance measurements of the municipality
- review the municipality's performance management system and make recommendations in this regard to the council.

#### **APPRECIATION**

31. The assistance rendered by the staff of the Nkomazi Local Municipality during the audit is sincerely appreciated.

*Auditor-General*

Nelspruit

30 November 2009



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*